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Washington, DC 20548

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June 28, 2002

The Honorable Paul Sarbanes  
Chairman  
The Honorable Phil Gramm  
Ranking Minority Member  
Committee on Banking, Housing, and Urban Affairs  
United States Senate

The Honorable Wayne Allard  
Ranking Minority Member  
Subcommittee on Housing and Transportation  
Committee on Banking, Housing, and Urban Affairs  
United States Senate

Subject: Community Investment: Los Angeles's Use of a Community Development  
Block Grant Exemption

Under the Department of Housing and Urban Development's (HUD) Community Development Block Grant (CDBG) program, entitlement communities<sup>1</sup>—also called grantees—receive funds that they can spend to support specific community development activities, such as rehabilitating housing, improving public facilities, and providing public services.<sup>2</sup> Most grantees are prohibited by statute from spending more than 15 percent of their CDBG funding on public service activities, such as child care, health care, and crime prevention. However, in the aftermath of the 1992 Los Angeles civil unrest, the Congress gave an exemption from this statutory cap to two grantees—the City of Los Angeles and the County of Los Angeles—allowing them to spend up to 25 percent of their funds on public services. In December 2001, the exemption was extended through 2003—this was the most recent in a series of extensions. Because of concerns about these two grantees' efforts to transition to the statutory levels for public service spending, you asked us to report on how the city and county (1) used their CDBG funding to provide public services during the

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<sup>1</sup>Entitlement communities are central cities of Metropolitan Statistical Areas, other metropolitan cities with populations of at least 50,000, and qualified urban counties with populations of at least 200,000 (excluding the populations of entitled cities). Entitlement communities develop their own programs and funding priorities.

<sup>2</sup>Public services include child care, health care, job training, recreation and education programs, public safety services, services for senior citizens and homeless persons, and drug abuse counseling and treatment. CDBG funding for public services is subject to several restrictions, such as a prohibition on funding services that were provided by the local government during the preceding 12 months.

## Report Documentation Page

<b>Report Date</b> 28JUN2002	<b>Report Type</b> N/A	<b>Dates Covered (from... to)</b> -
<b>Title and Subtitle</b> Executive Office of the President: Analysis of Mandated Report on Key Information Technology Areas	<b>Contract Number</b>	
	<b>Grant Number</b>	
	<b>Program Element Number</b>	
<b>Author(s)</b>	<b>Project Number</b>	
	<b>Task Number</b>	
	<b>Work Unit Number</b>	
<b>Performing Organization Name(s) and Address(es)</b> U.S. General Accounting Office 441 G Street NW, Room LM Washington, D.C. 20548	<b>Performing Organization Report Number</b> GAO-02-726r	
<b>Sponsoring/Monitoring Agency Name(s) and Address(es)</b>	<b>Sponsor/Monitor's Acronym(s)</b>	
	<b>Sponsor/Monitor's Report Number(s)</b>	
<b>Distribution/Availability Statement</b> Approved for public release, distribution unlimited		
<b>Supplementary Notes</b>		
<b>Abstract</b> see report		
<b>Subject Terms</b>		
<b>Report Classification</b> unclassified	<b>Classification of this page</b> unclassified	
<b>Classification of Abstract</b> unclassified	<b>Limitation of Abstract</b> SAR	
<b>Number of Pages</b> 17		

exemption period and (2) plan to transition from their current levels of public service spending to levels that meet the statutory 15 percent cap.

In response to your request, we analyzed HUD CDBG data, interviewed officials from HUD and the City and the County of Los Angeles, analyzed city and county data, and reviewed CDBG-related literature, as well as program information provided by HUD and local agency officials.<sup>3</sup> We did not specifically assess the city's or county's need for public services, or whether the grant funds were used in accordance with HUD, CDBG, or other federal guidelines. At times there was limited information available that addressed our objectives because there was no statutory or regulatory requirement that the grantees collect data or develop plans specifically associated with the exemption. We conducted our work in Washington, D.C., and San Francisco and Los Angeles, California, from January through June 2002, in accordance with generally accepted government auditing standards.

## **Results in Brief**

Between 1993 and 2001, the City of Los Angeles spent between 20 and 25 percent of its CDBG funding to support public service activities, while the County of Los Angeles spent between 9 and 20 percent. The city and county did not track how the additional allocation of funding for public service activities was spent, because they were not required to collect such data. According to HUD data for 1999 through 2001, the city and county used a majority of their public service funding to support general public services<sup>4</sup> and either youth or senior services. During this period, the City and the County of Los Angeles used different criteria to distribute public service funds geographically, and different techniques to allocate their funds to service providers.

There is no statutory or regulatory requirement that the grantees develop plans to transition to the 15 percent cap; however, HUD suggested in 1999 that the grantees develop such plans. As of May 2002, the City and the County of Los Angeles have undertaken some preliminary steps to facilitate a transition, but they do not have locally approved transition plans to decrease public service spending after 2003 in order to comply with the 15 percent spending cap. Both grantees requested, in separate reports submitted to Congress in 2000, that Congress make their exemption permanent because of persistent community needs. Both public agencies have undertaken some preliminary steps to facilitate a transition, but elected officials have not approved a transition plan. A transition plan would allow these agencies time to prioritize their spending, explore alternative funding sources, and notify the public of potential changes in available public services.

We are making a recommendation to HUD that the department request the city and county to submit locally approved plans to reduce their public service spending in the 2004 local fiscal year to the lower 15 percent statutory cap.

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<sup>3</sup>We did not independently verify the accuracy of the HUD, city, or county data and information provided.

<sup>4</sup>General public services include activities, such as neighborhood cleanup, food distribution, and rape prevention education that cannot be classified under a more specific category.

## Background

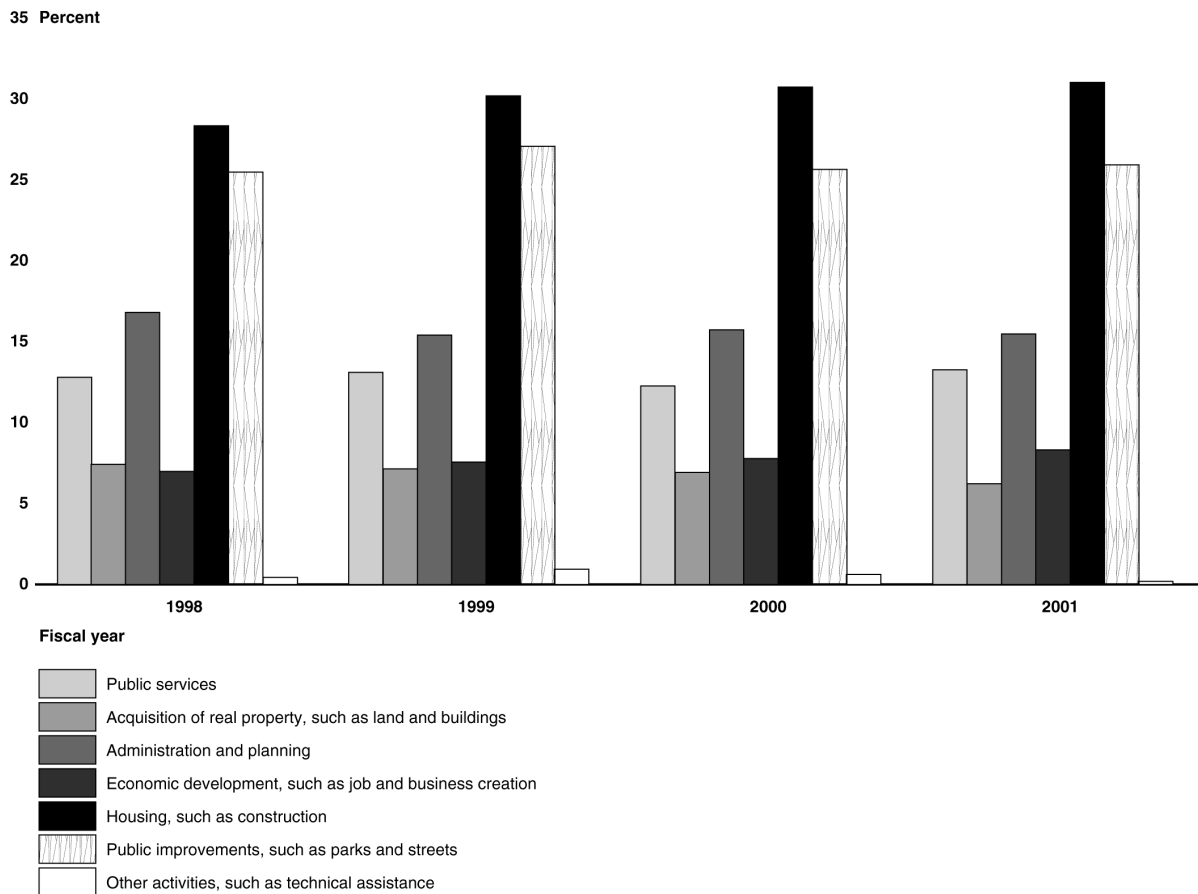
The CDBG program, created in 1974 to develop viable urban communities, is composed of several programs. One of these—the Entitlement Communities program—provides annual grants on a formula basis to cities and counties to carry out a wide range of community development activities directed toward providing decent housing, economic development, and improved community facilities and public services, principally for low- and moderate-income persons. Figure 1 shows the distribution of CDBG expenditures for this program by activity. To ensure that the CDBG Entitlement Communities program remained essentially a “physical development” program, Congress in 1981 capped the amount that grantees could spend for public services at 10 percent of their available grant funding.<sup>5</sup> This cap was subsequently increased to its current level of 15 percent, with exemptions for certain grantees.<sup>6</sup> Each grantee has the discretion to (1) determine the activities that will be funded in accordance with program regulations and (2) allocate funding to subrecipients—such as public or private nonprofit organizations or authorized for-profit entities—to carry out selected activities.

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<sup>5</sup>Pub. L. No. 97-35.

<sup>6</sup>Pub. L. No. 98-479 and Pub. L. No. 98-181 exempted grantees from the 15 percent cap if they used more than 15 percent of their CDBG funding for fiscal years 1982 or 1983 for public service activities. Consequently, about 41 of the 998 grantees are exempt from the 15 percent cap. Subsequent legislation in 1990, Pub. L. No. 101-625, allowed grantees to add program income received from the use of CDBG funds, such as from the sale or rent of property, to their grant amount, and to use the sum of the grant and the program income as the basis for calculating the amount that could be spent on public services.

Figure 1. Distribution of CDBG Expenditures among Categories of Eligible Activities, 1998-2001



Source: HUD.

Two grantees, the City of Los Angeles and the County of Los Angeles, administer the CDBG Entitlement Communities program in the south central Los Angeles area. The city's Community Development Department (city department) administers the city's CDBG program, while the Los Angeles County Community Development Commission (county commission) administers the county's program. These communities' elected officials—the mayor and city council, and the county board of supervisors—make the final decisions regarding the local implementation of the Entitlement Communities program. The city department both retains funds in order to provide services directly and allocates funds to subrecipients to provide other services. The county's CDBG program allocates funds to five supervisory districts covering unincorporated areas of the county and 48 participating cities that generally have populations of 50,000 or fewer, and those subrecipients select the activities to be carried out. Between 1993

and 2000, the city's CDBG grant increased from about \$77 million to \$90 million, while the county's grant increased from about \$37 million to \$38 million.<sup>7</sup>

In April and May 1992, Los Angeles experienced one of the largest instances of civil unrest<sup>8</sup> in the century, resulting in 42 deaths, \$1 billion in property damage, and 5,002 people arrested. An estimated 250 to 300 families lost their homes, more than 700 businesses were burned, and potentially 11,500 jobs were lost. Consequently, the City and the County of Los Angeles were declared federal disaster areas. Figure 2 shows the city and county boundaries and indicates the areas affected by the civil unrest. A 1992 report to the Los Angeles Board of Police Commissioners suggested that the causes of the unrest included racial and ethnic tensions, rapid demographic and economic changes, high unemployment, poverty, and the poor quality of local community-police relations.<sup>9</sup>

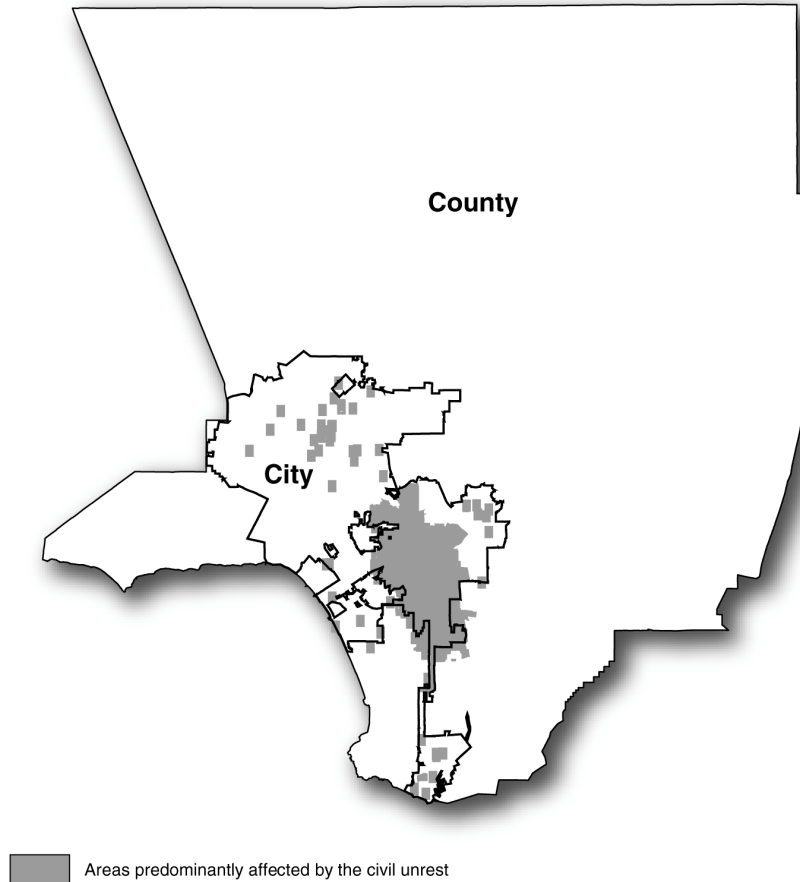
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<sup>7</sup>The dollar amounts and percentages listed for the City and the County of Los Angeles in this report have not been adjusted for inflation and describe various expenditures occurring during their local fiscal year (also referred to as "program year" or "grantee year"). The city's local fiscal year begins on April 1, while the county's local fiscal year begins on July 1. The city's local fiscal year for 1996 reflects 9 months of expenditures, because it changed its fiscal year from July 1 to April 1 that year.

<sup>8</sup>We use "civil unrest" to refer to the events that occurred in central and south central Los Angeles between April 29 and May 4, 1992. These events have been referred to by other terms, such as "riot."

<sup>9</sup>*The City in Crisis: A Report by the Special Advisor to the Board of Police Commissioners on the Civil Disorder in Los Angeles*, October 21, 1992.

Figure 2. Illustration Indicating the Boundaries of the City and the County of Los Angeles and Areas Predominantly Affected by 1992 Civil Unrest



Source: City and county officials, and *The City in Crisis: A Report by the Special Advisor to the Board of Police Commissioners on the Civil Disorder in Los Angeles*, October 21, 1992.

One of the actions Congress took in response to these events was to raise the 15 percent CDBG public service cap to 25 percent for fiscal years 1993 through 1997 for the City and the County of Los Angeles.<sup>10</sup> According to the House report that accompanied the proposed legislation,<sup>11</sup> the purpose for raising the cap was “to provide the city and county with critically needed funds to address both the immediate social service needs resulting from the civil unrest that occurred in April 1992, as well as the pervasive and underlying causes of such unrest.” The higher allocation of funding for public services would help fill the gaps created in program funding of various federal programs. Neither Congress nor HUD required any unique data or reports from the grantees during the original exemption period, 1993 through 1997. In 1993, HUD instructed the city and county to begin applying the 25 percent

<sup>10</sup>Pub. L. No.102-550.

<sup>11</sup>House Committee Report No. 102-760, House Committee on Banking, Finance, and Urban Affairs, July 30, 1992.

cap in their current local fiscal year cycle rather than in accordance with the federal fiscal year, in order to “immediately respond to the special situation relating to the riots.” Consequently, for 1993, the City of Los Angeles was able to spend up to about \$22 million on public services under the 25 percent cap instead of about \$13 million under the 15 percent cap, while the county was able to spend up to about \$12 million instead of \$7 million.

Congress extended the Los Angeles grantees’ CDBG exemption on public service spending in 1996, 1998, and 2000.<sup>12</sup> In the conference report accompanying the 1998 extension, the conferees noted their concern about continuing the extension beyond that fiscal year and directed HUD to provide a report describing what the city and county did with the additional public service funds and the nexus between the public service cap and the civil unrest for which the cap was waived.<sup>13</sup> HUD submitted these reports to Congress in October 2000. Although Congress repeatedly extended the original exemption, it did not provide any other guidance or impose any other requirements—apart from the nexus reports described above—on the grantees that related to their exemption from the 15 percent public service cap.

In response to the direction in the Conference Committee report and questions from the grantees, HUD provided guidance in February 1999 to the city and county to assist them in implementing the 1998 extension and in preparing the nexus reports. As part of this guidance, HUD interpreted the legislative history of the original exemption to mean that while the activities funded by the additional public service allocation need not be located in the civil unrest areas, they must address the results or underlying causes of the civil unrest. HUD indicated that the nexus reports should show a link between the public service activities supported in fiscal year 1999 by the additional 10 percent of allocated funding and the results or the causes of the civil unrest. HUD also indicated that they would not be “approving” the reports or identifying any corrective actions to be taken if program activities were not linked to the civil unrest.

CDBG grantees are required to develop both an annual CDBG program plan, which includes an opportunity for public comment, and a multi-year consolidated plan for all HUD funding, including the CDBG program. In its 1999 guidance to the city and county regarding the nexus reports, HUD also suggested that the city and county develop alternative plans for reducing the level of public services supported by CDBG funds for fiscal year 2000 and beyond in order to smooth the transition to the 15 percent cap.

In December 2001, the exemption was extended through 2003—this was the most recent in a series of extensions.<sup>14</sup> At that time, the Chairman and Ranking Members of the Senate Committee on Banking, Housing, and Urban Affairs and its

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<sup>12</sup>Pub. L. No.104-204; Pub. L. No.105-276; Pub. L. No.106-377.

<sup>13</sup>House Report No. 105-769, House Committee on Appropriations, October 5, 1998.

<sup>14</sup>Pub. L. No.107-116.

Subcommittee on Housing and Transportation indicated that they expected this to be the last extension of this exemption.<sup>15</sup>

### **Los Angeles Grantees Use Additional Public Service Funding to Address Community Needs**

During the exemption period (1993 to 2001), both the Los Angeles grantees spent over 15 percent of their CDBG funding on public service activities. While both the city and the county made use of the exemption, they used different criteria to distribute CDBG funding geographically and to allocate funds to subrecipients—other agencies or nonprofits—to provide the public services. The city distributed its CDBG funding geographically based on the poverty rate, and then used two funding techniques to allocate funds to subrecipients. In contrast, the county distributed funding geographically using a national CDBG formula, and then used one funding technique to allocate funds to subrecipients.

#### **City Spent 20 to 25 Percent of CDBG Funding on Public Services, While the County Spent 9 to 20 Percent**

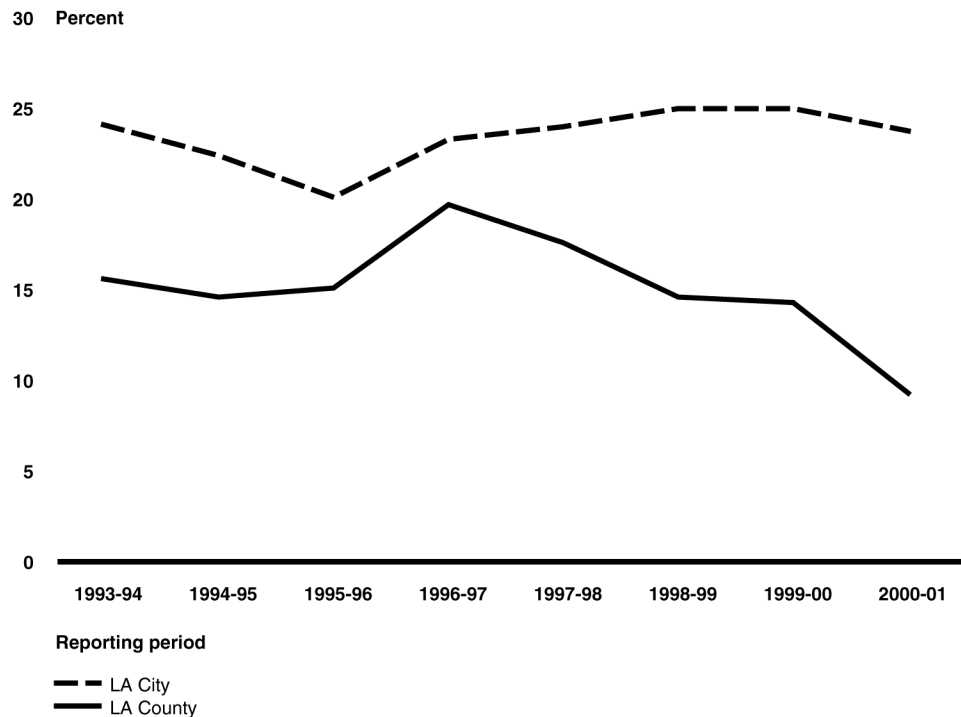
Between 1993 and 2001, the City of Los Angeles spent between 20 and 25 percent of its CDBG funding on public service activities.<sup>16</sup> During this same period, the County of Los Angeles spent between 9 and 20 percent of its CDBG funding on public service activities. During the period, the city spent over 20 percent in each reporting period, while the county spent about 15 percent or less in five of the eight reporting periods and never spent over 20 percent. Figure 3 illustrates the trends in the grantees' public service expenditures during this period. For three reporting periods, 1997 to 1998, 1998 to 1999 and 2000 to 2001, the county board initially required subrecipients to implement plans to spend at 15 percent because the commission was uncertain that the exemption would be extended. Although the exemption was subsequently extended, the county reported that the public service spending calculated under the cap for these reporting periods was 17.6, 14.6 and 9.3 percent, respectively. The county official suggested that these spending levels were attributable in part to the fact that participating cities tended not to readjust their public service spending once the program year began.

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<sup>15</sup>*Congressional Record*, vol. 147, no. 178, December 20, 2001, p. S13784.

<sup>16</sup>The data for the city and county reflect the expenditures reported under the public service cap. During the 1990s, changes in the CDBG program enabled a grantee to spend funds on public services through specific initiatives and not have these expenditures reported under the grantee's cap. For example, spending on public services carried out by community-based development organizations either as part of a specific initiative designed to increase economic opportunities through job training and support-service activities or as part of a strategy from a Neighborhood Revitalization Strategy Area might not count against the cap.

Figure 3. Trends in Public Service Expenditures, Reported as a Percentage of the Sum of the Entitlement Grant and Program Income for the City and the County of Los Angeles



Source: The City and the County of Los Angeles.

According to city department officials, in the first years after the civil unrest the department focused its public service spending on providing basic services, such as food and housing to residents affected by the civil unrest and the 1994 Northridge earthquake,<sup>17</sup> either directly or through subrecipients. During the exemption period, the city department funded the expansion of existing programs, such as a program to remove graffiti and discourage youth involvement in gangs and an after-school program for at-risk middle school children. In recent years, according to HUD data, the city department spent the majority of its CDBG public service funding providing general public services and youth services, as described in table 1.

<sup>17</sup>On January 17, 1994, an earthquake in Los Angeles measuring 6.8 on the Richter scale left 61 dead, 18,480 injured, and 25,000 homeless and caused \$13 billion in property damage. Los Angeles, Orange, and Ventura counties were declared federal disaster areas.

**Table 1: Distribution of City CDBG Funds Drawn for Selected Public Services, 1999–2001**  
(Dollars in millions)

Type of activity funded	Funds drawn in 1999		Funds drawn in 2000		Funds drawn in 2001	
	Amount	Percent	Amount	Percent	Amount	Percent
Public services (general)	\$9.37	36%	\$14.94	50%	\$12.70	34%
Youth services	8.25	31	6.13	20	9.64	26
Child care services	1.35	5	1.87	6	1.41	4
Health care services	1.38	5	1.67	6	1.29	3
Senior services	2.28	9	1.99	7	1.76	5
Employment training	.31	1	.06	0	3.96	11
Services for battered and abused spouses	.78	3	1.55	5	2.39	6
Operating costs of homeless and acquired immunodeficiency syndrome (AIDS) patients programs	0	0	0	0	1.96	5
Other public services	2.54	10	1.81	6	2.02	6
<b>Total funds drawn for public services</b>	<b>\$26.25</b>	<b>100%</b>	<b>\$30.00</b>	<b>100%</b>	<b>\$37.11</b>	<b>100%</b>

Notes: (1) Dollar amounts refer to funds drawn from the U.S. Treasury by the grantee, based on a line of credit. (2) Public services (general) include activities, such as neighborhood cleanup, food distribution, and rape prevention education that cannot be classified under a more specific category. (3) Percentages may not add to 100 percent due to rounding.

Source: HUD

In recent years, according to HUD data, the county disbursed the largest portion of its public service funding, between 60 and 66 percent, on general public service projects. The next highest portion of funding was disbursed among a variety of services, such as senior services and crime awareness services, as indicated in table 2.

**Table 2: Distribution of County CDBG Funds Drawn for Selected Public Services, 1999–2001**  
(Dollars in millions)

Type of activity funded	Funds drawn in 1999		Funds drawn in 2000		Funds drawn in 2001	
	Amount	Percent	Amount	Percent	Amount	Percent
Public services (general)	\$3.36	61%	\$3.07	54%	\$2.17	66%
Senior services	.49	8	.57	10	.24	7
Crime awareness	.40	7	.30	5	.14	4
Services for the disabled	.25	4	.29	5	.11	3
Youth services	.27	4	.24	4	.12	4
Operating costs of homeless and AIDS patients programs	.34	6	.42	7	.21	6
Other public services	.60	10	.80	14	.29	9
<b>Total funds drawn for public services</b>	<b>\$6.05</b>	<b>100%</b>	<b>\$5.68</b>	<b>100%</b>	<b>\$3.28</b>	<b>100%</b>

Notes: (1) Dollar amounts refer to funds drawn from the U.S. Treasury by the grantee, based on a line of credit. (2) Public services (general) include activities, such as neighborhood cleanup, food distribution, and rape prevention education that cannot be classified under a more specific category. (3) Percentages may not add to 100 percent due to rounding.

Source: HUD.

While CDBG public service expenditures for the county as a whole have fluctuated between 9 and 20 percent, county districts have typically spent between 15 and 25

percent of their CDBG funds on public services, according to a county commission official, and participating cities have spent between 10 and 15 percent. A commission official indicated that two of the five county districts include portions of the south central and east Los Angeles areas. These two districts have the highest poverty rate, and they tend to spend closer to 20 percent. Two other districts typically spend about 15 percent. The commission has allowed the last of the five districts, which annually receives a relatively small allocation—about \$150,000—to spend 100 percent of its CDBG funding on public services, because the county can offset higher public service allocations by the districts with the lower allocations by the cities.

Neither Congress nor HUD required the city and county to collect data or report on how they spent the additional 10 percent of allocated public service funding. As a result, the grantees could not readily quantify how much public service funding was spent on the specific results or causes of the 1992 civil unrest during the exemption period, from 1993 through the present. In commenting on a draft of this report, the city indicated that a significant portion of the additional allocation of public service funding was used to create two programs discussed later in this report. The city also provided information linking specific public service programs to general causes of civil unrest, as described in the McCone Commission and Kerner Commission reports,<sup>18</sup> such as unemployment, inadequate housing, and lack of education.

#### City and County Use Different Criteria and Methods to Allocate Public Service Funding

The City and the County of Los Angeles employ different strategies to allocate public service funding to subrecipients—other public agencies or nonprofits. The city allocates these funds to geographic areas of the city based on level of poverty, and then uses two funding methods to allocate funds to subrecipients. The county uses one of HUD’s national CDBG funding formulas to allocate funds to its subrecipients.

##### City Identifies Priorities, Employs Two Funding Methods

In the first few years after the unrest, the city department identified unmet community needs and problems in its delivery of services. A study, commissioned by the city department 6 months after the civil unrest, indicated that needs in the areas affected by the civil unrest arose from unemployment, crime, a high rate of school dropouts, ethnic or cultural tension, and other conditions, and that the barriers to using city services included a lack of awareness of services, fear, mistrust, language differences, and access. In 1998, a city task force recommended that the city department use an integrated, long-term approach to help families become self-sufficient; that is, not reliant on social services. In response to these findings and recommendations, the city established a new service delivery system that used both existing programs and new programs, such as youth and family centers and family

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<sup>18</sup>*The Kerner Report*, “The Issues of the Conditions of Our Nation’s Cities and Urban Communities across America Since the Riots that Occurred in Los Angeles 1 Year Ago,” the 1968 Report of the National Advisory Committee on Civil Disorders. Printed in 1968 and reprinted in the 1993 Hearing before the Committee on Banking, Housing, and Urban Affairs, United States Senate. *McCone Commission Report*, “Violence in the City: An End or A Beginning?” A Report of the Governor’s Commission on the Los Angeles Riots, 1965.

development networks, to provide integrated services and to help families become self-sufficient.

Since 1993, the city has also allocated social service funding throughout the city according to the level of poverty in each area, as determined by U. S. Census data. The areas of the city most affected by the civil unrest have received the highest portions of annual CDBG funding. A city official indicated that about 79 percent of CDBG public service funds are allocated and tracked by area. In 2000, about 33 percent of the funds allocated by area were allocated to the central area of the city, about 27 percent to the south area, about 16 percent to the San Fernando Valley area, and 11 percent to the east area. The remaining allocation, about 13 percent, was distributed to other areas of the city.

The city department both retains funds in order to provide services directly and allocates funds to subrecipients to provide services. The city department then uses both categorical and block grant funding techniques to allocate funding to its subrecipients. For example, in 2002, the city department allocated categorical funding in amounts ranging from about \$100,000 to over \$1 million to subrecipients to provide specific services, such as camp scholarships or AIDS prevention programs. It also allocates blocks of funding to subrecipients to provide integrated public services. For example, nonprofit consortiums operate family development networks that provide integrated services, such as case management and employment assistance to low-income residents. Each consortium annually receives between \$700,000 and \$800,000 to operate a network.

According to city department data for 2001, the city department retained about 7 percent of the public service funding and allocated about 35 percent to other city agencies and 58 percent to nonprofit organizations. Most of the nonprofit organizations funded by the city department were selected as a result of a competitive process.<sup>19</sup> The most recent request for proposals was conducted in 1999 in order to add new agencies or approaches.

### County Expands Existing Activities

According to a commission official, two of the five districts were marginally affected by the civil unrest and the participating cities were unaffected. County officials indicated that they did not link the allocation of the additional CDBG public service funding to addressing the causes of the 1992 civil unrest. County officials felt their existing programs were already helping address the general causes of civil unrest, as described in the McCone Commission and Kerner Commission reports. Consequently, the county's approach to using the higher allocation of public service funding was to expand its existing activities, such as employment training for lower-income persons, gang and youth delinquency prevention efforts, graffiti removal, community recreation, senior transportation services, and health services.

County commission officials indicated that, since 1975, the county has distributed the CDBG funding to its subrecipients using one of the CDBG formulas that HUD uses to

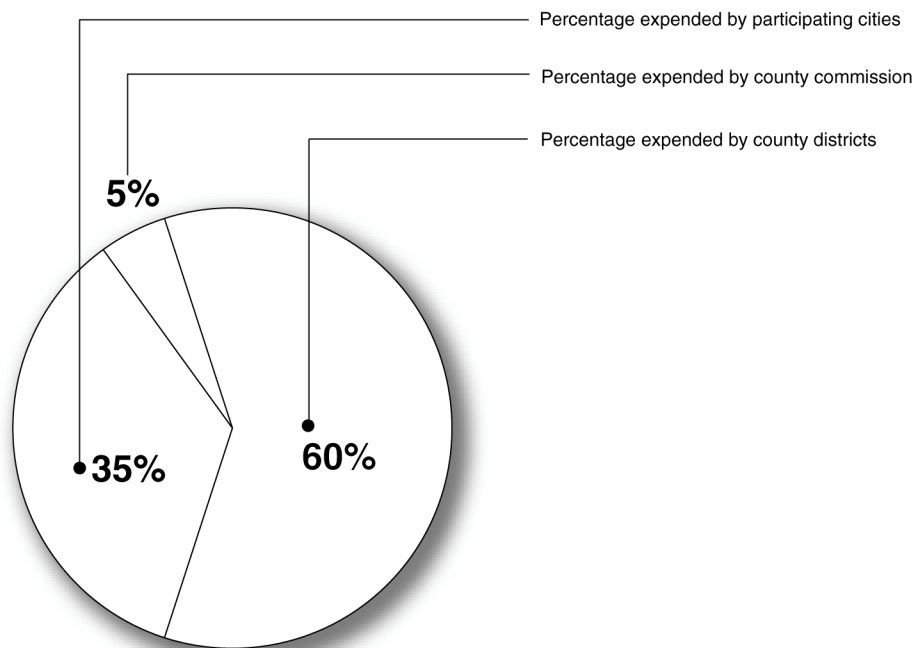
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<sup>19</sup>Grantees are not required to use a competitive process when contracting with nonprofit entities.

distribute the CDBG funds nationally. The county advises the districts and cities on, among other things, the planned allocations for public service spending. However, each district and participating city selects the public service activities to be carried out; selects the service provider, which can be a public agency or nonprofit organization; and determines the level of funding each activity receives. According to commission officials, the districts and cities generally do not coordinate with each other in service delivery. In the case of the districts, the commission carries out the districts' decisions, allocating funding to various selected service providers and monitoring provider performance. District supervisors select the nonprofit organizations that will be funded based on community needs and priorities, and on available funding.

Figure 4 illustrates the distribution of public service expenditures at the county commission, district and participating city levels in 1999. The county provided additional information about the distribution among nonprofits and public agencies at each level. Of the 60 percent of public services expended by the districts, nonprofits expended about 26 percent and public agencies expended about 34 percent. Of the 5 percent expended by the county commission, nonprofits expended about 1 percent and public agencies expended about 4 percent. Of the 35 percent of funding spent for public services by participating cities, nonprofits expended about 13 percent and public agencies expended about 22 percent.

Figure 4. Percentage of the County of Los Angeles' Expenditures of CDBG Public Service Funds in 1999, among Selected Subrecipients



Note: Periodically the commission uses unspent CDBG administrative funding to carry out countywide public service activities, such as nutrition counseling.

Source: The County of Los Angeles.

While the county relied on existing public service activities to meet community needs after the civil unrest, by 1997 the county was beginning to restructure its approach for identifying community needs. Historically, the county commission held community meetings, which were sparsely attended, to inform the public about the types of programs and projects that were under way. After 1997 the community meetings were used to solicit the public's perceptions of community needs, and the information gathered was included in developing the county commission's annual needs assessment. The county commission increased participation in its community meetings and implemented some of the top priorities identified through its community outreach efforts.

### **City and County Take Initial Steps to Reallocate CDBG Spending**

As of May 2002, the City and the County of Los Angeles did not have approved transition plans to decrease public service spending by 2004 in order to comply with the 15 percent spending cap. Both public agencies have undertaken some preliminary steps to facilitate a transition, but elected officials have not approved a transition plan. Both grantees have requested that Congress make their exemption permanent because of persistent community needs.

A city department official indicated that the mayor and city council have not approved a written plan specifically describing how they would transition from their 25 percent cap to the program's 15 percent cap. The official also noted that they have tried to anticipate such a development and have planned accordingly. For instance, the city department requires nonprofits, through the 1999 request for proposals process, to provide 20 percent matching plans and to describe their contingency plans in the event of receiving reduced funding from the city. In addition, the city department's planning document states that the city strongly encourages collaboration among its funded agencies to limit administrative costs and maximize program funds. A city official suggested that in order to comply with the 15 percent cap, the city might cut funding across all activities. Officials from several of the other city agencies that were subrecipients of CDBG public service funding indicated that they were unsure of how they would adjust their activities if the CDBG public service funding were reduced.

County commission officials indicated that in order for the county to comply with a 15 percent cap, they would, as they had in the past, instruct their recipients to plan on spending 15 percent or less on public services. Specifically, the county board of supervisors approved plans to spend at 15 percent in 1997, 1998, and 2000. A county official indicated that the county advised its subrecipients to develop contingency plans to increase public service spending to 25 percent in the event that the exemption was extended and to focus additional public service spending on items that would be useful after an extension period ended, such as computer equipment and supplies. Although a limited number of new programs were created during the exemption period, in general, the county commission did not want to depend on the higher public service allocation in the event that the public service cap reverted to 15 percent. The county added that, to transition to the 15 percent cap, it also could consider exempting smaller nonprofit organizations if the nonprofits were not able to function as a result of the funding cut.

## Grantees Request Permanent Exemption

In response to the 1998 request for nexus reports, the city and county submitted their reports to HUD in the spring of 2000. In these reports, the city and county requested that their 25 percent public service cap exemption become permanent. Both reports suggested that the underlying general causes of civil unrest still affected many of their communities. The city based its request on its need to support long-term self-sufficiency programs, especially in the neighborhoods affected by the civil unrest, and on the increasing demand for human services. The county stressed that it had been difficult to engage in broad, long-range planning regarding the use of the additional 10 percent allocation for public services when it had been repeatedly unclear in recent years that the exemption would be extended. City and county officials indicated that the general causes of civil unrest—such as unemployment, inadequate housing, and lack of education—continued to the present. Legislative advocates for both the City and the County of Los Angeles indicated in May 2002 that both grantees were continuing their efforts to obtain a permanent exemption from Congress.

## **Conclusions**

As HUD suggested in 1999, developing plans to reduce spending from the 25 percent cap would smooth the transition to the lower, 15 percent cap in the event that the exemption is not extended. More specifically, developing and approving transition plans would (1) give the public agencies and subrecipients time to prioritize spending and explore alternative funding sources and (2) notify the public of potential changes in available public services. Because the city has consistently spent closer to the 25 percent cap than the county, a sudden transition to the 15 percent cap might prove more disruptive to residents and service providers in the city than in the county. Although city department officials have undertaken some preliminary steps to facilitate a transition in the event that the exemption is not extended, elected officials have not approved a plan for the transition. The county has implemented plans in the past to spend at 15 percent, and officials indicated that implementing a transition plan to a 15 percent cap would not be difficult. However, the county does not have an approved transition plan to reduce their public service spending in their 2004 local fiscal year.

## **Recommendation for Executive Action**

To help ensure a smooth transition in the event that the 25 percent public service cap is not extended, we recommend that the Secretary of Housing and Urban Development request that officials from the City and the County of Los Angeles submit locally approved plans to reduce their public service spending in the 2004 local fiscal year to the lower, 15 percent statutory cap.

## Agency Comments

We provided a draft of this report for review and comment to HUD and to the City and the County of Los Angeles. HUD generally agreed with the information presented. City of Los Angeles officials generally agreed with the information presented and provided some additional information, which was included where appropriate.

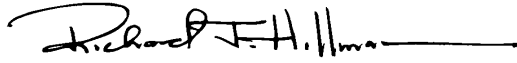
Officials from the County of Los Angeles raised several concerns about the report. First, they felt that the information provided did not adequately describe how they disseminated the CDBG funds among the county districts and participating cities. Specifically, county commission officials suggested that we report on their planned public service expenditures, which in the years under review tended to be higher than the actual amount spent by the districts and the participating cities. Officials indicated that the county planned to spend higher amounts on public services; but the districts and the participating cities, which have the discretion to spend funds on specific public service activities, controlled actual expenditures. Consequently, the actual expenditures varied from planned expenditures, especially when the exemption was approved late in their local fiscal year. However, we used the annual public service expenditures, as reported by the grantees, because HUD uses those expenditures to determine compliance with the public service cap. Second, the commission officials felt our recommendation that HUD request the county to submit a transition plan was unnecessary, since the county had implemented spending at 15 percent in 3 different years during the exemption period. While the county has implemented a transition plan in the past, we believe that it would be beneficial for the county's subrecipients, nonprofit service providers, and residents to be advised of the county's plans for 2004. Also, if the county's elected officials intend to employ the same strategy as they have in the past, then developing such a plan at HUD's request would not be an undue burden. Third, because the views of the Chairmen and Ranking Members of the Senate Committees were not included as statutory language or in congressional reports, the county said that it plans to continue to advocate for the extension of the cap.

Officials from HUD, the city, and the county offered a number of technical or clarifying comments that we incorporated throughout the report as appropriate.

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We are sending copies of this letter to the Secretary of HUD and to the City and the County of Los Angeles. We will make copies available to others on request. The letter is also available at no charge on our Web site at <http://www.gao.gov>.

If you have any questions about this report, please contact Nancy Simmons, Assistant Director, or me at (202) 512-8678. Key contributors to this assignment were Patricia Farrell Donahue, Janet Fong, Tracy Guerrero, and Andrea Rogers.

A handwritten signature in black ink, reading "Richard J. Hillman", followed by a horizontal line.

Richard J. Hillman  
Director, Financial Markets  
and Community Investment